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C O N F I D E N T I A L SANAA 001959

SIPDIS

PLEASE PASS TO MCC FOR A. BAYLOR

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SUBJECT: SALEH AUTHORIZES ECONOMIC REFORMS: ROYG BRACES FOR DEMONSTRATIONS

REF: SANAA 1919

Classified By: CDA Nabeel Khoury for reasons 1.4 b and d.

11. (C) Summary. On July 18, President Saleh approved long-delayed portions of the economic reform package. A reduction or elimination of the fuel subsidy is likely to accompany this decision, and some fear it will lead to civil unrest. Several reports indicate that the security forces will employ harsh tactics to control demonstrations should they erupt. The ROYG canceled permits for the diplomatic community to travel outside the capital city for "the next few days." Lifting of the fuel subsidy may result in the scapegoating and possible removal of prominent government officials, first among them, the Minister of Finance. End summary.

ROYG Prepares to Employ "Strict Measures"

12. (C) Interior Minister Alimi recommended that foreign diplomats remain in Sanaa and restricted their in-country travel for the next few days for fear of demonstrations to the lifting oil subsidies (reftel). All ROYG ministers and many other officials have been instructed not to leave the country. Removal of oil subsidies is highly unpopular with Yemenis. There is as yet no word about the exact timing of price hikes in fuel, but indications point to the next few days.

13. (C) A source at the Ministry of Interior said President Saleh summoned police officials to his palace to prepare for civil unrest. He handed out riot batons to those in attendance, raised one above his head, and instructed them to use force in the event of demonstrations.

Economic Reform: "The Sweet Before the Bitter"

14. (SBU) Removal of the fuel subsidy was preceded by passage of three key elements of the long awaited economic reform package. In the words of a UN official, the ROYG "supplied the sweet before the bitter." On July 18, Saleh issued presidential decrees authorizing the general sales tax (GST), the customs tariff law, and the law for employment, wages, and salaries. The new GST law reflects the input of business leaders in private meetings with Saleh, and will come in the form of a five percent levy on all imported and locally produced goods (reftel). The law represents a major departure from the IMF-WB recommended value added tax and passed by Parliament exempting basic goods including wheat, rice, medicine, baby milk, raw gold, and cashing money. Tobacco products, qat, weapons, phone service, and jewelry will be taxed at different rates.

15. (SBU) The Customs Tariff Law ratifies amendments to the Customs Law that bring Yemen's tariffs in line with the World Customs Organization, a positive step toward WTO accession. The Employment, Wages, and Salaries System Law re-classifies salaries and provides pay increases to public employees compatible with a minimum wage and above the poverty line. The law is part of a larger program of civil service reform, headed by the Ministry of Civil Service, which proposes to reduce government payroll and increase efficiency.

Top Ministers May Pay the Price

16. (C) Comment: Speculation is the subsidies will be lifted on Friday afternoon (July 22), when most Yemenis have already returned home from prayer and are the least likely to take to the streets. Minister Alimi told CDA that the opposition is on board with the reforms but that there is no guarantee they will not call for the demonstrations anyway, adding, "Maybe you can help us with them!" The lifting of subsidies may also be used to conduct a long-anticipated cabinet shake-up, depending on the strength of the public reaction. Prominent figures such as Prime Minister Bajamal may take the fall for an unpopular Presidential decision. According to prominent businessman Fatti Fahem, Minister of Finance Salami,

currently receiving medical attention in Frankfurt, has
already unofficially resigned. End comment.
Khoury